

Singapore Company Guide

Sembcorp Industries

Version 27 | Bloomberg: SCI SP | Reuters: SCIL.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

19 May 2020

HOLD

Last Traded Price (18 May 2020): S\$1.55 (STI : 2,523.55)
Price Target 12-mth: S\$1.70 (10% upside) (Prev S\$2.20)

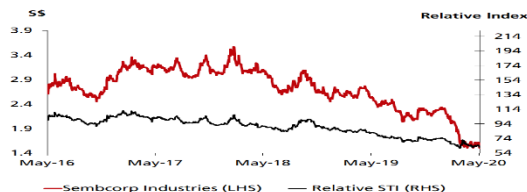
Analyst

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What's New

- Challenging 2020 though confident to churn positive operating cash flow
- Energy & Marine businesses affected by COVID-19
- Urban segment expected to delivery steady profits
- FY20/21F earnings cut by 15%/7%; Maintain HOLD; TP lowered to S\$1.70

Price Relative



Forecasts and Valuation

FY Dec (\$m)	2018A	2019A	2020F	2021F
Revenue	11,689	9,618	8,865	8,901
EBITDA	1,379	1,488	1,535	1,614
Pre-tax Profit	420	295	429	480
Net Profit	347	247	321	390
Net Pft (Pre Ex.)	345	412	321	390
Net Pft Gth (Pre-ex) (%)	(31.5)	19.3	(22.2)	21.7
EPS (S cts)	19.4	13.8	17.9	21.8
EPS Pre Ex. (S cts)	19.3	23.0	17.9	21.8
EPS Gth Pre Ex (%)	(31)	19	(22)	22
Diluted EPS (S cts)	19.3	13.7	17.8	21.7
Net DPS (S cts)	4.00	5.00	4.49	5.46
BV Per Share (S cts)	380	384	397	415
PE (X)	8.0	11.2	8.6	7.1
PE Pre Ex. (X)	8.0	6.7	8.6	7.1
P/Cash Flow (X)	3.7	2.8	3.6	3.3
EV/EBITDA (X)	9.2	8.6	8.3	7.8
Net Div Yield (%)	2.6	3.2	2.9	3.5
P/Book Value (X)	0.4	0.4	0.4	0.4
Net Debt/Equity (X)	1.1	1.1	1.1	1.1
ROAE (%)	5.1	3.6	4.6	5.4
Earnings Rev (%):			(15)	(7)
Consensus EPS (S cts):			19.9	23.4
Other Broker Recs:		B: 5	S: 2	H: 5

Source of all data on this page: Company, DBS Bank, Bloomberg Finance L.P

Defensive but not immune

Maintain HOLD; TP lowered to S\$ 1.70, as we factor in a lower valuation for marine and reduced our earnings projections. While Sembcorp Industries (SCI) is already trading at a steep 50% discount to book, re-rating potential hinges on ROE enhancement (from current ~5%) stemming from earnings recovery of its utilities businesses in India and the UK and marine segment. Potential restructuring between SCI and Keppel Corp remains a wild card.

Key re-rating catalyst: Emerging markets as long-term growth engines. SCI's India operations swung from a loss of S\$58m in FY17 to a profit of S\$32m (excl. one-offs) in FY19, and growth ahead would help to drive overall group earnings. The power market in India seems to be recovering with the current peak surplus expected to reverse by FY20, according to independent research house CRISIL, and drive up tariffs. Besides India, SCI has also made forays into other emerging markets – Bangladesh, Vietnam and Myanmar.

Where we differ: We hold on to our view of a potential merger between Keppel's O&M arm and Sembcorp Marine (SMM) given the keen competition in the sector. We believe a spin-off of its marine arm could re-rate SCI's undervalued utilities business that is being overshadowed by the cyclical marine business. However, this event could take another year or so to materialise.

Valuation:

We derive our fair value for SCI based on the sum of its different parts, with a 10% conglomerate discount to the RNAV, to arrive at a TP of S\$1.70. This represents 0.5x P/BV.

Key Risks to Our View:

Key risks to earnings are further delays in marine contract wins, deterioration of Singapore's power spark spreads, and execution hiccups at its Indian power plants.

At A Glance

Issued Capital (m shrs)	1,786
Mkt. Cap (S\$m/US\$m)	2,768 / 1,951
Major Shareholders (%)	
Temasek Holdings Pte Ltd	49.5
Free Float (%)	50.5
3m Avg. Daily Val (US\$m)	8.0
GIC Industry : Industrials / Capital Goods	



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WHAT'S NEW

1Q20 business update

Expect positive operating cash flow in 2020. SCI remains confident to **maintain positive operating cash flow** in 2020 underpinned by its long-term contracts and diversified portfolio of businesses, even though COVID-19 has hit its operations to some extent.

Energy not spared. While its Energy segment which includes power and wastewater treatment, are relatively more resilient, mostly backed by long-term contracts, the reduction in economic activity due to lockdowns in multiple markets has affected merchant operations, leading to a decrease in energy demand and prices particularly in Singapore, India, and the UK. **Power demand in April 2020 has declined by 10-25% y-o-y for these markets.**

With this downtrend expected to continue for the rest of the year, performance of the **Energy business in 2020 is expected to be markedly lower** than 2019.

In addition, we could see **one-off items** including:

1) Currency losses on its Chile divestment, which is expected to complete in 3Q20. The accumulated currency translation loss was S\$30m as of end 2019.

2) Potential inventory loss resulting from ~40% plunge in energy prices, which has significantly reduced the net realisable value (NRV) of inventory of gasoil reserves in Singapore that is required to fulfil certain regulatory requirements. As at Mar-2020, the NRV is estimated to be S\$59m, representing a S\$45m (pre-tax) reduction in book value.

Urban expected to provide steady core profits in 2020 despite near term slowdown. The pace of land and property sales for the Urban business has been affected by the COVID-19 pandemic with government measures to contain the virus and delays in regulatory approvals. The uncertain economic outlook could also lead to lower take-up and demand, or delayed launches for some of the business' integrated developments and properties. Notwithstanding these, the Urban business is expected to **generate steady recurring profits** in 2020 underpinned by its orderbook.

Marine on Survival mode; losses to continue. In SMM's outlook statement, it stressed that in light of the challenging and deteriorating business environment, the current priority is to ensure adequate liquidity to sustain operations and ride through this severe downturn. The group will continue to focus on safety and timely execution of projects and explore pockets of opportunities less affected by the current business climate. It expects **losses to continue** in the foreseeable quarters.

Earnings forecast revised lower: We trimmed our FY20/21F earnings by 15%/7% to reflect the weaker marine and energy businesses in 1H20. We have yet to factor in one-offs that could arise.

CRITICAL DATA POINTS TO WATCH

Critical Factors

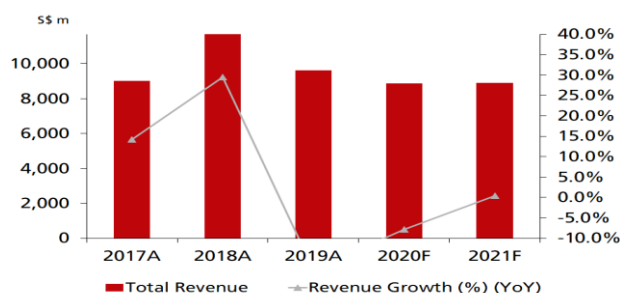
Energy earnings recovery. We expect earnings recovery for Energy business post COVID-19 disruption. For Energy in India, Sembcorp Energy India Limited (SEIL) - SCI's first Indian power plant (SEIL Project 1) - is starting to contribute more steadily at S\$15-20m a quarter to the bottom line. Meanwhile, losses at its second plant (SEIL Project 2) should narrow to a near-breakeven level with load factor & tariff improvements, as well as commencement of long-term PPA in Bangladesh in February 2019 (19% of capacity) and in Andhra Pradesh hopefully in 2020 (38% of capacity).

Energy in emerging markets remain the growth engine. SEIL operates 4,294MW of power capacity comprising 2,640MW of thermal power and 1,654MW of renewable capacity. Management targets to grow renewable capacity in India by 300-500MW p.a. Besides India, SCI has also made forays into other emerging markets – Bangladesh, Vietnam and Myanmar – and this should underpin the longer-term growth prospects of its Energy segment beyond 2019. Both Myanmar's 230MW gas-fired Myingyan Independent Power Producer (IPP) and Bangladesh's 427MW gas-fired Sirajganj Unit 4 commenced operations in 1H19 and should contribute maiden full year profits in 2020.

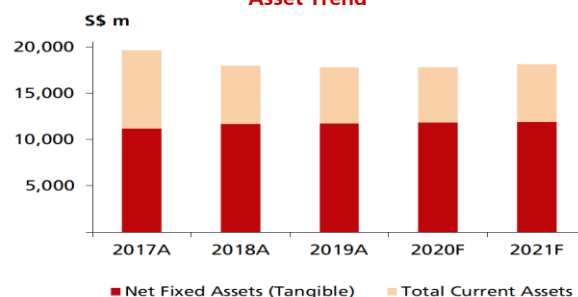
Marine business (SMM) earnings are orderbook-driven. We expect setback in order wins recovery in 2020 due to COVID-19, lower oil prices and capex cuts. We estimate order wins to hover around 2019's level of S\$1.5bn this year. As a recap, order wins hit a low of ~S\$300m in FY16 before trending up to S\$1bn / S\$1.2bn / S\$1.5bn in FY17 / FY18 / FY19. New project pipeline includes the new Gravifloat modularised LNG terminal solutions, renewable and FPSO projects. SMM's orderbook stood at S\$2.4bn as at Dec-2019. This translates into a book-to-bill ratio of 1x based on the existing delivery schedule. For Marine, we expect losses to narrow these two years driven by cost savings.

Urban Development business provides growth opportunities. Urban Development accounts for c.20% of SCI's bottom line on average but its earnings tend to be lumpy. A strong performance from this segment may not move the needle too much for now but represents an avenue for growth. SCI has about 423 ha across China, Indonesia and Vietnam to be booked over the next 2-3 years.

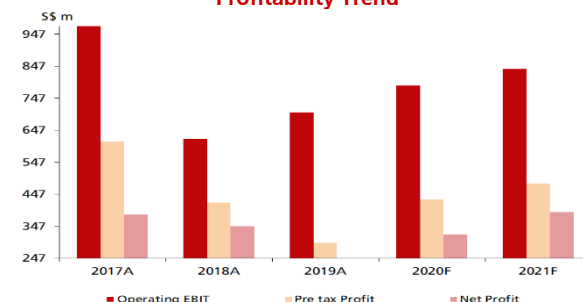
Sales Trend



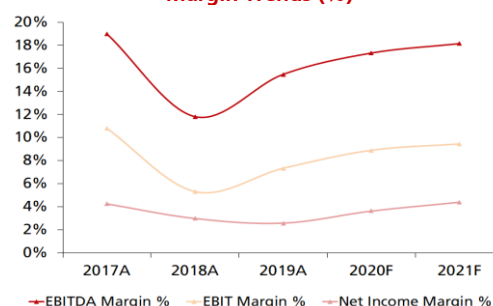
Asset Trend



Profitability Trend



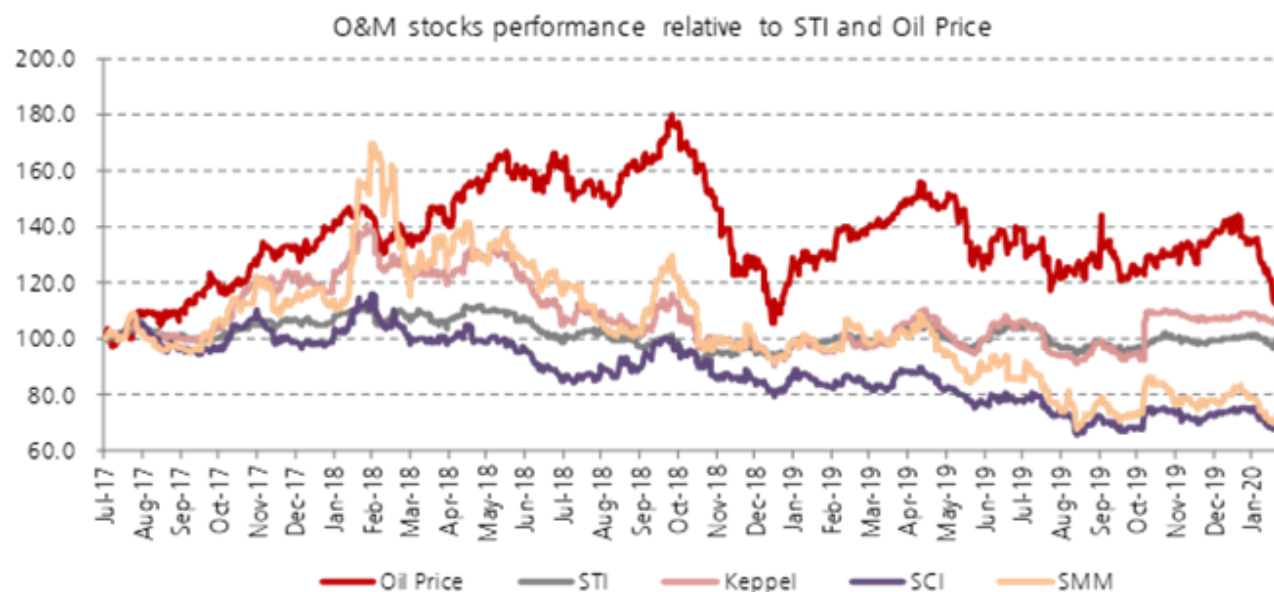
Margin Trends (%)



Source: Company, DBS Bank

Appendix 1: A look at Company's listed history – what drives its share price?

Sembcorp Industries' Share Price has underperformed Oil Price and STI



Source: Company, DBS Bank, Bloomberg Finance L.P.

Sembcorp Industries' P/B vs ROE; turnaround of SEIL Project 2 and Marine are key earnings and ROE drivers



Source: Company, DBS Bank, Bloomberg Finance L.P.

Sembcorp Industries

Balance Sheet:

SCI's net gearing inched up slightly to 1.2x as at Dec-2019.

SCI's current gearing position is in stark contrast to its net cash position in 2013 due to increasing leverage at SMM and expansion into India.

Share Price Drivers:

Oil price rebound would drive SCI's share price higher. Investors would have greater confidence in the Marine business as the operating environment improves. Orders for production-related facilities are expected to flow through post COVID-19.

Marine order wins and Urban Development land sales bode well for SCI's share price. While the oil price rebound would be an early indicator, SMM securing contract wins is more tangible. More momentum in land sales would signal more hope for growth and be positive to its share price.

Widening spark spreads at India and Singapore power plants.

Signs of positive and widening spark spreads in India and Singapore would alleviate a key concern of investors.

Key Risks:

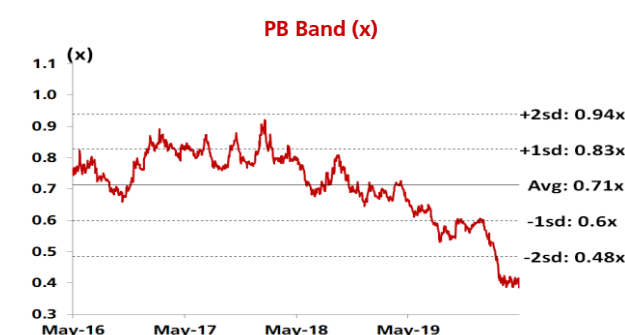
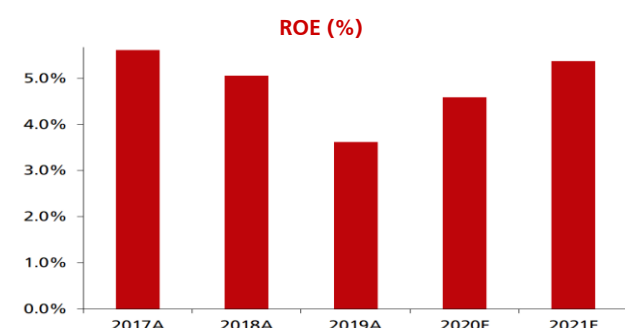
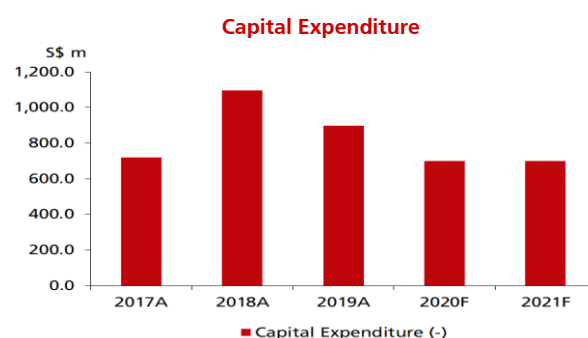
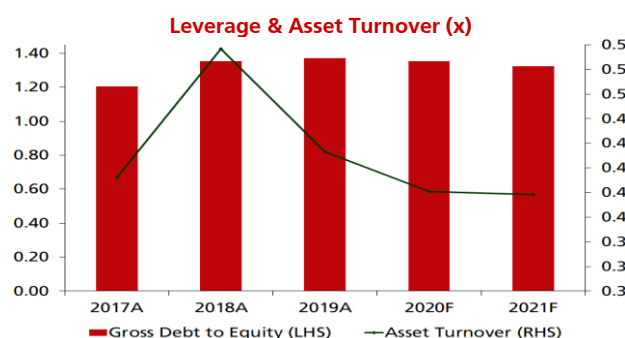
Execution of Indian power plants. The availability of coal supply and tariff fluctuation for SCI's power plants in India are concerns. We find comfort that the SEIL Project 1 is up and running, with 86% of capacity committed on long-term PPAs and operating using both domestic and imported coal. SEIL Project 2 has also shown signs of recovery with ~19% of capacity under long-term PPAs in 2019 and potentially another 38% in 2020.

Environment, Social, Governance:

SCI has long held a strong commitment to sustainability by enabling a low-carbon and circular economy, empowering the company's people and communities and embedding responsible business practices. In 2018, SCI was once again selected as an index component of both the Dow Jones Sustainability Asia Pacific Index and the SGX Sustainability Leaders Index.

Company Background

Sembcorp Industries (SCI) is a trusted provider of essential energy and water solutions to both industrial and municipal customers. It has facilities with over 11,000MW of gross power capacity and over 9m cubic metres of water per day in operation and under development. It is also a world leader in marine and offshore engineering (via Sembcorp Marine [SMM]) as well as an established brand name in urban development (comprising industrial parks as well as business, commercial and residential space) in Vietnam, China and Indonesia.



Source: Company, DBS Bank

Key Assumptions

FY Dec	2017A	2018A	2019A	2020F	2021F
Marine contract wins	1,000	1,200	1,500	1,500	3,500

Segmental Breakdown

FY Dec	2017A	2018A	2019A	2020F	2021F
Revenues (\$m)					
Energy	5,697	6,536	6,138	6,249	6,336
Marine	3,035	4,888	2,883	2,354	2,328
Urban	7.76	5.00	280	7.39	8.87
Other Businesses and	280	260	317	254	228
Total	9,020	11,689	9,618	8,865	8,901
Net Profit before EI					
Energy	140	312	195	266	325
Marine	6.83	(48.0)	(85.0)	(24.8)	(7.3)
Urban	83.2	86.0	117	70.2	77.2
Other Businesses and	0.68	(3.0)	20.0	9.00	(5.0)
Total	231	347	247	321	390
Net Profit before EI					
Energy	2.5	4.8	3.2	4.3	5.1
Marine	0.2	(1.0)	(2.9)	(1.1)	(0.3)
Urban	1,072.8	1,720.0	41.8	949.5	870.4
Other Businesses and	0.2	(1.2)	6.3	3.5	(2.2)
Total	2.6	3.0	2.6	3.6	4.4

Income Statement (\$m)

FY Dec	2017A	2018A	2019A	2020F	2021F
Revenue	9,026	11,689	9,618	8,865	8,901
Cost of Goods Sold	(7,735)	(10,769)	(8,602)	(7,628)	(7,636)
Gross Profit	1,291	920	1,016	1,236	1,266
Other Opng (Exp)/Inc	(320)	(302)	(313)	(450)	(427)
Operating Profit	972	618	703	787	839
Other Non Opg (Exp)/Inc	30.0	40.0	27.0	(7.8)	(7.8)
Associates & JV Inc	164	174	184	153	150
Net Interest (Exp)/Inc	(434)	(414)	(454)	(503)	(501)
Exceptional Gain/(Loss)	(121)	1.79	(165)	0.0	0.0
Pre-tax Profit	611	420	295	429	480
Tax	(118)	(88.0)	(78.0)	(125)	(106)
Minority Interest	(110)	15.0	30.0	16.1	16.1
Preference Dividend	0.0	0.0	0.0	0.0	0.0
Net Profit	383	347	247	321	390
Net Profit before Except.	504	345	412	321	390
EBITDA	1,712	1,379	1,488	1,535	1,614
Growth					
Revenue Gth (%)	14.2	29.5	(17.7)	(7.8)	0.4
EBITDA Gth (%)	26.4	(19.5)	7.9	3.2	5.1
Opg Profit Gth (%)	28.5	(36.4)	13.7	11.9	6.6
Net Profit Gth (Pre-ex) (%)	23.8	(31.5)	19.3	(22.2)	21.7
Margins & Ratio					
Gross Margins (%)	14.3	7.9	10.6	13.9	14.2
Opg Profit Margin (%)	10.8	5.3	7.3	8.9	9.4
Net Profit Margin (%)	4.2	3.0	2.6	3.6	4.4
ROAE (%)	5.6	5.1	3.6	4.6	5.4
ROA (%)	1.7	1.5	1.1	1.4	1.7
ROCE (%)	4.2	2.5	2.6	2.8	3.2
Div Payout Ratio (%)	23.3	20.6	36.2	25.0	25.0
Net Interest Cover (x)	2.2	1.5	1.5	1.6	1.7

Source: Company, DBS Bank

Quarterly / Interim Income Statement (\$\$m)

FY Dec	4Q2018	1Q2019	2Q2019	3Q2019	4Q2019
Revenue	2,566	2,480	2,372	2,450	2,316
Cost of Goods Sold	(2,338)	(2,213)	(2,107)	(2,213)	(2,069)
Gross Profit	228	267	265	237	247
Other Oper. (Exp)/Inc	(95.9)	(89.0)	(87.0)	(77.0)	(60.0)
Operating Profit	132	178	178	160	187
Other Non Opg (Exp)/Inc	40.0	0.0	0.0	0.0	27.0
Associates & JV Inc	39.6	45.0	54.0	41.0	44.0
Net Interest (Exp)/Inc	(116)	(108)	(115)	(117)	(114)
Exceptional Gain/(Loss)	1.00	0.0	0.0	0.0	(165)
Pre-tax Profit	95.9	115	117	84.0	(21.0)
Tax	12.9	(18.0)	(15.0)	(24.0)	(21.0)
Minority Interest	(2.7)	(4.0)	(4.0)	11.0	27.0
Net Profit	106	93.0	98.0	71.0	(15.0)
Net profit bef Except.	105	93.0	98.0	71.0	150
EBITDA	211	223	232	201	258

Growth

Revenue Gth (%)	(15.1)	(3.3)	(4.4)	3.3	(5.5)
EBITDA Gth (%)	(6.8)	5.5	4.0	(13.4)	28.4
Opg Profit Gth (%)	(30.6)	35.2	0.0	(10.1)	16.9
Net Profit Gth (Pre-ex) (%)	13.6	(11.5)	5.4	(27.6)	111.3

Margins

Gross Margins (%)	8.9	10.8	11.2	9.7	10.7
Opg Profit Margins (%)	5.1	7.2	7.5	6.5	8.1
Net Profit Margins (%)	4.1	3.8	4.1	2.9	(0.6)

Balance Sheet (\$\$m)

FY Dec	2017A	2018A	2019A	2020F	2021F
Net Fixed Assets	11,158	11,672	11,739	11,837	11,904
Invt in Associates & JVs	1,765	1,741	1,696	1,779	1,859
Other LT Assets	2,330	3,584	3,722	3,722	3,722
Cash & ST Invt	2,687	1,925	1,767	1,961	2,235
Inventory	3,548	1,864	1,977	1,773	1,780
Debtors	2,094	2,289	2,048	1,927	1,935
Other Current Assets	163	246	303	303	303
Total Assets	23,745	23,321	23,252	23,302	23,738
ST Debt	1,572	1,862	2,643	2,643	2,643
Creditor	3,340	2,968	2,844	2,621	2,632
Other Current Liab	1,421	746	525	432	414
LT Debt	8,275	8,870	8,157	8,307	8,457
Other LT Liabilities	963	937	1,204	1,204	1,204
Shareholder's Equity	6,944	6,788	6,871	7,102	7,412
Minority Interests	1,230	1,150	1,008	992	976
Total Cap. & Liab.	23,745	23,321	23,252	23,301	23,738
Non-Cash Wkg. Capital	1,044	685	959	950	973
Net Cash/(Debt)	(7,160)	(8,807)	(9,033)	(8,989)	(8,865)
Debtors Turn (avg days)	81.9	68.4	82.3	81.8	79.2
Creditors Turn (avg days)	171.1	112.6	132.1	142.0	136.9
Inventory Turn (avg days)	178.1	96.6	87.3	97.4	92.6
Asset Turnover (x)	0.4	0.5	0.4	0.4	0.4
Current Ratio (x)	1.3	1.1	1.0	1.0	1.1
Quick Ratio (x)	0.8	0.8	0.6	0.7	0.7
Net Debt/Equity (X)	0.9	1.1	1.1	1.1	1.1
Net Debt/Equity ex MI (X)	1.0	1.3	1.3	1.3	1.2
Capex to Debt (%)	7.3	10.2	8.3	6.4	6.3
Z-Score (X)	1.0	1.1	1.0	1.0	1.0

Source: Company, DBS Bank

Cash Flow Statement (\$m)

FY Dec	2017A	2018A	2019A	2020F	2021F
Pre-Tax Profit	611	420	295	429	480
Dep. & Amort.	571	595	682	602	632
Tax Paid	(69.9)	(122)	(99.0)	(204)	(125)
Assoc. & JV Inc/(loss)	(164)	(174)	(184)	(153)	(150)
Chg in Wkg.Cap.	(791)	(389)	(379)	88.8	(3.8)
Other Operating CF	494	409	662	0.0	0.0
Net Operating CF	651	739	977	763	833
Capital Exp.(net)	(718)	(1,096)	(898)	(700)	(700)
Other Invt.(net)	206	(421)	(64.0)	0.0	0.0
Invt in Assoc. & JV	37.8	(19.0)	0.0	0.0	0.0
Div from Assoc & JV	307	167	229	70.0	71.0
Other Investing CF	75.8	152	282	0.0	0.0
Net Investing CF	(92.0)	(1,217)	(451)	(630)	(629)
Div Paid	(162)	(100.0)	(91.0)	(89.4)	(80.2)
Chg in Gross Debt	779	854	121	150	150
Capital Issues	0.0	0.0	0.0	0.0	0.0
Other Financing CF	(363)	(1,013)	(697)	0.0	0.0
Net Financing CF	253	(259)	(667)	60.6	69.8
Currency Adjustments	(8.0)	(25.0)	(17.0)	0.0	0.0
Chg in Cash	804	(762)	(158)	194	274
Opg CFPS (\$ cts)	80.7	63.1	75.9	37.7	46.8
Free CFPS (\$ cts)	(3.8)	(20.0)	4.42	3.52	7.45

Source: Company, DBS Bank

Target Price & Ratings History



Note: Share price and Target price are adjusted for corporate actions.

Source: DBS Bank

Analyst: Pei Hwa HO

DBS Bank recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

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Sources for all charts and tables are DBS Bank unless otherwise specified.

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